

**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554**

In the Matter of)	
Review of the Commission's Rules)	
Regarding the Pricing of Unbundled)	Docket No. WC 03-173
Network Elements and Resale of Service)	
by Incumbent Local Exchange Carriers)	

**Reply Comments of the Staff of the
New Jersey Board of Public Utilities**

I. INTRODUCTION

The Staff of the New Jersey Board of Public Utilities (NJBPU Staff) submits the following reply comments in response to the Federal Communications Commission's (FCC) Notice of Proposed Rulemaking (NPRM) issued in the above referenced docket on September 15, 2003.¹ In its NPRM, the FCC announced its intentions to initiate its first comprehensive review of its rules for the pricing of Unbundled Network Elements (UNEs), which were adopted pursuant to the Telecommunications Act of 1996 (the 1996 Act). In its 1996 *Local Competition Order*,² the FCC adopted the Total Element Long Run Incremental Cost (TELRIC) methodology as a means to promote local exchange competition.

TELRIC by design was intended to set prices for UNEs at rates that would mimic pricing in a fully competitive market. To accomplish this, the FCC built in certain forward-looking assumptions that assumed that the price for network elements would be based on costs that assume that wire centers will be placed at the incumbent LEC's current wire center locations, but that the reconstructed local network will employ the most efficient technology for reasonably foreseeable capacity requirements.³ TELRIC has

¹ *In re: Review of the Commission's Rules Regarding the Pricing of Unbundled Network Elements and the Resale of Service by Incumbent Local Exchange Carriers*, Federal Communications Commission, WC Docket No. 03-173 (rel. Sept. 15, 2003) (NPRM).

² *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, CC Docket No. 96-98, First Report and Order, 11 FCC Rcd 15499 (1996) (*Local Competition Order*), *aff'd in part and vacated in part sub nom. Comp. Tel. Assoc. v. FCC*, 117 F.3d 1068 (8th Cir. 1997) and *Iowa Utils. Bd. v. FCC*, 120 F.3d 753 (8th Cir. 1997), *aff'd in part and remanded*, *AT&T v. Iowa Utils. Bd.*, 525 U.S. 366 (1999); *on remand Iowa Utils. Bd. v. FCC*, 219 F.3d 744 (8th Cir. 2000), *reversed in part sub nom. Verizon Communications, Inc. v. FCC*, 535 U.S. 467 (2002).

³ Local Competition Order at 985.

been used since its approval in 1996 by all state commissions in their proceedings to determine proper UNE prices, and has subsequently been upheld by the U.S. Supreme Court.⁴

The FCC states that in this initial comprehensive review of TELRIC it “seeks comments on tentative conclusions and proposed modifications to the current UNE pricing regime that seek to preserve its forward-looking emphasis and its pro-competitive purposes, while making it more transparent and theoretically sound.”⁵ In this proceeding, the FCC “proposes to simplify TELRIC pricing, while simultaneously improving the accuracy of its pricing signals, by resolving one of the key internal tensions that marks its current application: the assumption that for some purposes, rates should reflect a market with widespread facilities-based competition but, for other purposes, rates should reflect a market with a single dominant carrier.”⁶ The FCC’s stated objective of the NPRM is “to modify or clarify the Commission’s rules in order to help *state commissions more easily develop UNE prices and resale discounts* that meet the statutory standards established by Congress in section 252(d) and to provide more certainty and consistency in the results of these state proceedings.”⁷

Pursuant to the NPRM, initial comments were filed on December 16, 2003 by over 30 parties, including Incumbent Local Exchange Carriers (ILECs), Competitive Local Exchange Carriers (CLECs), state regulatory commissions, including the National Association of Regulatory Utility Commissioners (NARUC)⁸ and consumer agencies.

As an initial matter, the NJBPU Staff generally supports the concepts articulated by NARUC in its initial comments. In its comments, NARUC argued that the FCC should retain TELRIC pricing of UNEs because the methodology has not only held up against court challenges, but because it has been a factor in encouraging and sustaining local competition. In addition, NARUC points out that, in its current form, TELRIC provides states with the needed flexibility to address state-specific conditions and that any revisions contemplated by the FCC should consider whether they provide states with the

⁴ *Verizon Communications, Inc. v. FCC*, 535 U.S. 467 (2002) (*Verizon v. FCC*).

⁵ NPRM at ¶ 4.

⁶ NPRM at ¶ 4.

⁷ NPRM at ¶ 9.

⁸ Comments of the National Association of Regulatory Utility Commissioners, James Bradford Ramsey, NARUC General Counsel, December 16, 2003.

flexibility to address local concerns. We also agree with NARUC's position that states should retain the right to establish state-specific fill factors that vary from the ILEC's actual fill factors and the flexibility to employ an adjustment factor, but one developed in the context of a state proceeding.⁹

II. DISCUSSION

A. Retain the use of TELRIC pricing

As noted above, comments were filed in this proceeding by regulatory commissions in several states, including, Iowa, Illinois, Missouri, New York, Pennsylvania and Texas. In addition to NARUC, comments were also filed by the New Jersey Division of the Ratepayer Advocate and the National Association of State Utility Consumer Advocates (NASUCA). Although the comments differ in certain respects among the various agencies, there is consensus from all parties that the FCC should retain the use of TELRIC in determining appropriate UNE pricing.

The FCC acknowledges in its NPRM that TELRIC has withstood previous legal challenges:

The Supreme Court in *Verizon v. FCC* affirmed our choice of TELRIC as a permissible methodology for states to use in ratemaking proceedings. The court held that the Commission's decision to adopt a forward-looking cost methodology was a reasonable interpretation of the statute and that the Commission did not err in rejecting alternative methodologies advocated by the incumbent LECs. The court also rejected arguments that various aspects of the TELRIC methodology were unlawful.¹⁰ (citations omitted).

As noted by the FCC, since 1996, almost every state, including those who filed comments, has conducted ratemaking proceedings to establish UNE prices using the TELRIC methodology.¹¹ The vast experience gained by state commissions in these proceedings has provided the commissions with extensive knowledge in the usefulness of the TELRIC methodology.

⁹ Id. at 1.

¹⁰ NPRM at ¶ 5.

¹¹ NPRM at ¶ 6.

The FCC noted its concern over the fact that numerous state proceedings have produced significant differences in rates from state to state for given carriers, which it believes could indicate that the process is not meeting the FCC's goal of sending appropriate economic signals.¹² However, as noted by the New Jersey Division of the Ratepayer Advocate in its comments, these criticisms were flatly rejected by the Supreme Court in *Verizon v. FCC*. States have used the TELRIC methodology over the last seven years to effectively meet the two goals of the FCC for UNE pricing: 1) to ensure UNE prices are "set in a manner that sends efficient entry and investment signals to all competitors", and 2) "provide ILECs an opportunity to recover the forward looking costs of providing UNEs."¹³ The fact that all of the state commissions agree that TELRIC should be retained serves as a true testament to the usefulness of the TELRIC methodology in the state's role in setting appropriate UNE prices, and should be recognized by the FCC as such.

B. Ensure any revisions to TELRIC methodology will provide states with flexibility needed to reflect state-specific conditions.

As noted above, one of the objectives of the FCC in this review is to streamline the FCC's rules to assist state commissions to more easily develop UNE prices.¹⁴ The FCC acknowledges in its NPRM the difficult task which states have faced in attempting to establish forward looking UNE rates using the TELRIC methodology, including several lengthy proceedings to review extensive and at times complicated testimony, cost models, and accompanying inputs.¹⁵ These proceedings have been a necessary exercise to allow states to properly examine the proofs of costs presented by the various parties and cost models for these individual states, and to ensure that UNE costs are set properly within the TELRIC standards. The "wide latitude" which the FCC references that states are provided in applying the "most efficient technology" standard under the current TELRIC rules is precisely what the FCC must preserve in any revisions of the TELRIC methodology. Although the NJBPU Staff supports the FCC's goal of assisting state commissions generally, we concur with the position of the Pennsylvania Public Utility Commission (PA PUC), that the FCC should not impose additional mandates on UNE

¹² NPRM at ¶ 6.

¹³ NPRM at ¶ 38.

¹⁴ NPRM at ¶ 9.

¹⁵ NPRM at ¶ 6.

pricing which in effect “restrict a State commission’s ability to exercise informed judgment based on the circumstances presented by the parties.”¹⁶ The NJBPU Staff, however, is concerned that any attempt by the FCC to assist states by making the UNE pricing process easier, may come at a high cost by eliminating state authority to address local concerns. Loss of state control could potentially impede or diminish inroads that state commissions have achieved since 1996.

Permitting states to retain flexibility in UNE pricing is consistent with some of the FCC’s proposals in its NPRM. For example, the FCC concludes in the NPRM that UNE prices should be based on costs more firmly rooted in the real world attributes of the existing ILEC’s network rather than the hypothetical network used as the basis for the TELRIC methodology.¹⁷ As noted in the *Resolution on the FCC’s TELRIC Rulemaking* submitted by NARUC in its comments, “the FCC’s focus in the NPRM on considering real world attributes in the development of forward-looking costs may be consistent with the approaches taken in many States.” The ability of states to consider real world attributes is an inherent part of the flexibility now provided to states under the current rules to consider real world state-specific conditions. Thus, permitting states to retain their flexibility in setting UNE rates will most likely assist the FCC in its goal to decrease the hypothetical nature of the TELRIC methodology, and refine the process using more real world attributes. States must continue to have flexibility in determining proper UNE prices to effectively fulfill the significant role bestowed to them under the statutory obligations of the 1996 Act.

C. Permit states to determine adjustment factors for rate changes over time, and retain the discretion to conduct full UNE pricing proceedings.

The FCC seeks comment in the NPRM on whether there might be mechanisms that could be used to adjust UNE prices over time, thereby reducing the need for state commissions to conduct a full UNE pricing proceeding every few years.¹⁸ The NJBPU Staff concurs with NARUC’s comments that any such mechanism or adjustment factor should properly be designed within the context of a state TELRIC cost docket. Having dealt with UNE pricing issues for the last seven years, state commissions are the most

¹⁶ Comments of the Pennsylvania Public Utility Commission at 4 (PAPUC Comments).

¹⁷ NPRM at ¶ 52.

¹⁸ NPRM at ¶¶ 138-140.

logical and knowledgeable party to ascertain how to appropriately calculate an adjustment factor that would meet the goals of providing proper economic incentives for competition. As noted by NASUCA in its comments:

“[s]tates . . . have extensive knowledge of the details of state markets, telecommunications infrastructure and the economy. State regulators have extensive experience analyzing cost models for the purpose of setting prices, and are well positioned to examine the facts, and make the detailed decisions that are required for determining reasonable UNEs.”¹⁹

However, notwithstanding the existence of such an adjustment factor, states must also retain the discretion to conduct a full UNE pricing proceeding, should they deem it necessary. State commissions retain their legal obligation under the 1996 Act to determine UNE rates, and therefore, should also retain the discretion to conduct a full UNE pricing proceeding to properly meet its commitments. As acknowledged above, state regulators are best able to determine when it is appropriate, and provide the appropriate venue for determining UNE rates, where the concerns of all interested parties are properly considered.²⁰ As noted by the New York Department of Public Service, the decision whether to undertake a new UNE proceeding rests correctly in the hands of regulators, who are closest to the market involved: “There is no reason to require states and the parties to bear significant costs when states such as New York, have little incentive to allow significantly out-of-date UNE rates to continue without review.”²¹ The Iowa Utilities Board properly concludes in their comments: “Just as state commissions should be allowed to determine costs and set their own rates independently, they should also be allowed to determine appropriate adjustment factors and levels based upon the particular circumstances in each state.”²²

The FCC seeks comments in the NPRM on the appropriate guidelines for states to follow in establishing fill factors, and asks whether the ILEC’s fill factors should be dispositive, in light of the FCC’s conclusion to more closely account for real world attributes in its TELRIC analysis.²³ As noted above, state commissions are best equipped to determine what factors are appropriate to properly determine UNE rates.

¹⁹ NASUCA comments at 18.

²⁰ NASUCA comments at 18.

²¹ Comments of the New York Department of Public Service at 14. See also Ratepayer Advocate comments at 6.

²² Comments of the Iowa Utilities Board at 6.

²³ NPRM at ¶73-75.

Requiring that the state commission use the ILEC's fill factor could create conflict with the ability of the State commission to determine what fill factor is appropriate based upon the TELRIC methodology, as well as the state specific conditions. The FCC's decision to include more real world attributes in its analysis of UNE rates must be realistically balanced with the ability of the state commissions to determine what fill factors will meet the FCC's ultimate goal of providing proper economic incentives for competition. As noted by the PA PUC, the FCC must be careful to not implement a pricing methodology which is overly complex or rigid, lest the role of the State commission in the establishment of UNE rates is reduced to a "fill in the blank" exercise that eliminates the exercise of the informed judgment of the states. Therefore, the NJBPU Staff concurs with NARUC's comments that states should retain the ability to use a different fill factor than that of the ILEC, to maintain their ability to properly implement the goals of the 1996 Act to generate facilities based competition.

III. CONCLUSION

The NJBPU Staff supports the objectives of the FCC in its thorough review of the TELRIC UNE pricing rules to assist state commissions in its statutory duty to properly set UNE rates. With the extensive knowledge that state commissions have gained over the past seven years, they remain the prime catalyst for stimulating competition in the local exchange market. The FCC must work together with the state commissions to provide guidance, rather than mandates, which will help bring all parties to the intended goals where the general economy, competitors and consumers reap the benefits of a fully competitive marketplace.

There can be no question that those most affected by the FCC's UNE pricing rules are the individual states and consumers. Therefore, state commissions must retain the flexibility not only to promote the FCC's stated goals and objectives, but also the latitude to continue to pursue the state policies and objectives that we have all invested so heavily in. Loss of the authority to react to state specific conditions may in fact hinder the very goals that the FCC purports to promote.

Respectfully submitted,

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